

Research, SBIR, and the Small Business Technology Transfer, STTR, program because it requires federal agencies with at least a \$100 million research and development, R&D, budget to set aside a certain percentage of awards for small firms. The SBIR program was created in 1982 because small businesses—the most innovative sector of our economy—received very few R&D awards. Almost the entire federal R&D budget back then went to large firms and academic institutions.

There are many good provisions in H.R. 5819. Section 102 increases the small business set-aside in the SBIR program from 2.5 percent to 3 percent. The SBIR awards come in three phases—Phase I is for start-ups; Phase II is for follow-on work; and Phase III is for commercialization of the product either in the form of government procurement or for sale in the marketplace. Section 103 increases the maximum award in Phase I from \$100,000 to \$750,000. For Phase II awards, the maximum award goes up from \$300,000 to \$2.2 million. There are no grant dollars for the Phase III or commercialization phase. In the past, few federal agencies had any interest in Phase III. However, H.R. 5819 contains several provisions, most particularly in Title IV, to encourage commercialization of products developed with SBIR awards.

However, Section 201 of H.R. 5819 opens up more of the SBIR program to small firms that have significant investments from venture capital (VC) companies. For the purposes of the SBIR program, a small firm would be considered to be independently owned and operated even with a majority share owned by VC firms. VC investments, unlike a bank loan, make the “owner” of the company no longer the true leader of the firm if venture capitalists own more than 50 percent of the firm. In other words, he or she doesn’t control the ultimate destiny or direction of the company—the “owner” has to take ultimate direction from the VC firms. The small business is no longer independently owned and operated. Thus, if a small company receives venture capital even from multiple sources to pursue Vaccine A but then sees the research going in a different direction to develop Vaccine B, the “owner” of the company will be compelled to complete the research on Vaccine A for which he or she received funding unless the “owner” receives permission from the venture capitalists to pursue Vaccine B.

The only limitations on VC investments in Section 201 for SBIR firms are that (1) no one single VC firm can own a majority of the tech company applying for a SBIR grant; (2) the VC firm does not control a majority of the seats on the tech company’s board of directors; (3) only “small” VCs, as defined in the bill as those VC firms employing 500 employees or less, can participate; and (4) a “corporate-owned” VC firm can only own up to 10 percent of a SBIR tech company and that a SBIR tech company can only have one investment from a corporate VC. My concerns are that the first two limitations can be easily evaded by creative VCs that set up multiple firms. The third limitation dealing with a small business definition of a VC encompasses almost every VC in the nation. The Small Business Administration (SBA) currently defines small venture capital firms as those with less than \$6.5 million in annual receipts. There is no need to change the small business definition of a VC.

In Section 110, H.R. 5819 also allows firms to apply directly for Phase II awards, bypassing the Phase I process. In my opinion, combining three key elements of H.R. 5819—dramatically higher awards (Section 103), allowing almost every VC in the nation to own more than a majority of a SBIR firm (Section 201), and bypassing Phase I (Section 110)—sets up a stage where VC-owned “small” firms will gobble up most of the money in the SBIR program. Then, there would be a dramatic drop-off in the number of truly very small and independently-owned companies in the SBIR program, particularly those looking for Phase 1 start-up funding.

During my tenure as Chairman of the House Small Business Committee, I spent a lot of time and effort trying to solve the specific problem of the eligibility of some small businesses with venture capital investments to participate in the SBIR program at the National Institutes of Health (NIH). After the Defense Department, the NIH is the second-largest spender of R&D funding in the federal government. This issue of the role of VC investment in SBIR companies seems primarily confined to NIH.

Section 201 in H.R. 5819 tries to solve a problem that is grossly exaggerated. It is a myth that small businesses with VC investments are unable to participate in the SBIR program at NIH because of a misinterpretation of the law by the SBA. In an impartial Government Accountability Office (GAO) study that was released in 2006, the GAO discovered that 17 percent of NIH SBIR awards, accounting for 18 percent of the dollar value, went to small businesses with VC investments in Fiscal Year 2004. These small firms had no problem in complying with SBA guidelines. Nevertheless, I tried to proffer a compromise to establish a two-year pilot SBIR-like program to set-aside 0.5 percent of NIH R&D funding for smaller firms that receive a preponderance of their funding from VCs and do not own or control their company. Unfortunately, my compromise was rejected by NIH and by the biotech and VC industries. However, the solution contained in Section 201 is a dramatic overreach in the effort to solve this specific problem with NIH.

Finally, the Bush Administration shares my concern on this issue. According to the Statement of Administration Policy issued on April 22, 2008, “the Administration believes that H.R. 5819 goes too far in relaxing constraints on venture capital ownership of firms receiving SBIR and STTR funds, which could lead to inappropriate subsidization of well-capitalized businesses that do not warrant funding through a set-aside program. The Administration is reviewing whether venture capital funding of businesses receiving SBIR and STTR funds could be expanded through reforms of SBA regulations without inappropriately providing Federal commercialization subsidies to well-capitalized businesses.”

Thus, for these reasons, I urge my colleagues to oppose H.R. 5819.

Ms. ESHOO. Madam Chairman, I rise today in support of H.R. 5819, the SBIR/STTR Reauthorization Act.

The Small Business Innovation Research, SBIR, and Small Business Technology Transfer, STTR, programs are important sources of Federal support to facilitate the commercialization of research. Updating these programs will ensure the continuation of the central role they

play in maintaining the preeminence of the U.S. research enterprise.

The importance of fostering public-private partnerships cannot be underestimated. I see firsthand all the aspects of the innovation process, because my Congressional district contains basic research institutions, hundreds of current and former SBIR- and STTR-awarded companies, and venture capital firms. The SBIR and STTR programs facilitate the transition of technologies to the market. The important changes made by this reauthorization include increasing the award guideline levels, establishing advisory boards to improve program effectiveness and outcomes, and emphasizing the importance of energy-related research proposals.

A key aspect of the debate surrounding this reauthorization has been whether or not venture capital-backed companies should be eligible to participate in the SBIR program. Small businesses with a proven ability to attract venture funding should not be excluded.

The original legislation which created the program stated that no federal funds could be used for the Phase 3 commercialization state of an SBIR award, requiring award recipients to seek venture capital and other private sector funding. Preventing those companies from returning to the program for a different project undermines its very objective of bringing more technologies to the market. A small business that wins an SBIR and then attracts VC funds has a proven ability to succeed, yet may have insufficient resources to pursue new research projects. These companies should be eligible to continue to participate in the program and I’m pleased to see that the reauthorization before us today maintains this position.

Let me remind my colleagues that Congress did not authorize a policy change to prohibit venture-backed companies from participating in the program. A ruling by an SBA administrative law judge made this interpretation and seriously damaged the program by disqualifying many good companies. Today we clarify the language and get the SBIR program back on the right track, without excluding small businesses which have successfully obtained venture capital funding for other technologies.

I know there are concerns that this bill’s increase in the percentage of research funds that are directed to the SBIR and STTR programs will detract from the core research missions of the agencies. This is a particular concern for the NIH which has been working under a constrained budget over the last several years. We need to continue to increase funding at the NIH and other research agencies, and we should consider the impact of increasing the SBIR and STTR set-aside as the bill moves forward in the legislative process.

I hope the House will demonstrate strong bipartisan support for this bill to ensure that the innovators and entrepreneurs of our country continue to have Federal assistance to transition their research and ideas out of the labs and into the marketplace. I urge the entire House to support this important legislation.

Mrs. JONES of Ohio. Madam Chairman, I rise today in support of H.R. 5819, a bill that will reauthorize the Small Business Innovation Research—SBIR, and Small Business Technology Transfer, STTR, programs through 2010.

I support these programs because they provide a much needed boost in business innovation and job creation throughout the country.